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IN THE

Supreme Court of the United States.

GEORGE M. WEST CO., Appellant,

vs.

LEA BROS. & CO., Appellees.

ON CERTIFICATE FROM THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH DISTRICT.

BRIEF FOR GEORGE M. WEST COMPANY,
by W. W. HENRY, Counsel.

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This is a case of petitioning creditors in involuntary bankruptcy against the appellant, which had made a general deed of assignment and offered a plea of solvency.

The question submitted to this court by the Circuit Court of Appeals of the Fourth District is in the following words (top p. 5 of Record): "Whether or not a plea that the party against whom the petition was filed 'was not insolvent as defined in the bankrupt act at the term of the filing of the petition against him,' is a valid plea in bar to a petition in bankruptcy filed against a debtor who has made a general deed of assignment for the benefit of his creditors."

ARGUMENT.

Under the Bankrupt Act of 1867 there was much discussion and various decisions, as to the meaning of the word "insolvency," as used in that act. The Supreme Court, in *Toof* v. *Martin*, 13 Wall., p. 47, said: "The term insolvency is not always used in the same sense. It is sometimes used to denote the insufficiency of the entire property and assets of an individual to pay his debts. This is its general and popular meaning. But it is also used in a more restricted sense, to express the inability of a party to pay his debts as they become due in the ordinary course of business. It is in this latter sense that the term is used when traders and merchants are said to be insolvent, and as applied to them it is the sense intended by Congress."

Congress, in passing the act now in force, determined to restrict the meaning of the term in all cases, to its general and popular sense, and in Section 1 (15) provided that: "A person shall be deemed insolvent within the provisions of this act, whenever the aggregate of his property, exclusive of any property which he may have conveyed, transferred, concealed or removed, or permitted to be removed or concealed, with intent to defraud, hinder or delay his creditors, shall not, at a fair valuation, be sufficient in amount to pay his debts." And under (19) defined the word "persons" to indicate "corporations, officers, partnerships," &c. The meaning of this definition of "insolvency" seems plainly, that it requires that the assets of the alleged insolvent must be insufficient, at a fair valuation, to pay his debts, exclusive of any property he may have conveyed, &c., with intent to defraud, hinder or delay his creditors. That is, in case he has made such conveyance, the property so conveyed shall be excluded from the estimate of his assets. Any other meaning, such as was contended for in the District Court by the appellees, would restrict the use of the word "insolvent," when used in the act, to the case of a person who had made a fraudulent conveyance, and no other

person, however insufficient his assets to pay his debts, could be deemed insolvent, in contemplation of this act; which is contrary to reason, and does violence to the language of the act.

The law of 1867 (amended in 1874) recites in Sec. 39, a number of acts which, when committed, made the debtor liable to be made an involuntary bankrupt. An examination of these shows that many of them do not necessarily require insolvency; but the acts being admitted, or being found by a jury to have been committed, the debtor was adjudged a bankrupt. (See *Wilson* v. *City Bank*, 17 Wal., 473, which cites the section). By the act now in force Congress determined to change this, and in all cases of proceedings in involuntary bankruptcy to require both insolvency, and acts of bankruptcy on behalf of the debtor, to enable the petitioning creditors to succeed in throwing him into bankruptcy. Following the decision in *Buckingham* v. *McLean*, 13 How., 446, and others to the same purport, the act clearly distinguishes between insolvency and bankruptcy. The first makes it insufficiency of assets to pay debts, the second, an adjudicated status of the debtor, based on certain acts which may, or may not, involve insolvency. This is apparent from the following citation from section 3 of chapter 111 of the act:

a. "Acts of bankruptcy by a person shall consist of his having (1) conveyed, transferred, concealed, or removed, or permitted to be concealed or removed, any part of his property with intent to hinder, delay or defraud his creditors, or any of them; or (2) transferred, while insolvent, any portion of his property to one or more of his creditors, with intent to prefer such creditors over his other creditors; or (3) suffered or permitted, while insolvent, any creditor to obtain a preference through legal proceedings, and not having at least five days before a sale or final disposition of any property affected by such preference vacated or discharged such preference; or (4) made a general assignment for the benefit of his creditors; or

(5) admitted in writing his inability to pay his debts and his willingness to be adjudged a bankrupt on that ground.

b. "A petition may be filed against a person who is insolvent and who has committed an act of bankruptcy within four months after the commission of such act. Such time shall not expire until four months after (1) the date of the recording or registering of the transfer or assignment when the act consists of having made a transfer of any of his property with intent to hinder, delay, or defraud his creditors or for the purpose of giving a preference as hereinbefore provided, or a general assignment for the benefit of his creditors, if by law such recording or registering is required or permitted, or, if it is not, from the date when the beneficiary takes notorious, exclusive, or continuous possession of the property, unless the petitioning creditors have received actual notice of such transfer or assignment.

c. "It shall be a complete defense to any proceedings in bankruptcy instituted under the first subdivision of this section, to allege and prove that the party proceeded against was not insolvent as defined in this act, at the time of the filing the petition against him, and if solvency at such date is proved by the alleged bankrupt, the proceedings shall be dismissed, and under said subdivision one the burden of proving solvency shall be on the alleged bankrupt.

d. "Whenever a person against whom a petition has been filed as hereinbefore provided under the second and third subdivisions of this section, takes issue with and denies the allegation of his insolvency, it shall be his duty to appear in court on the hearing, with his books, papers and accounts, and submit to an examination, and give testimony as to all matters tending to establish solvency or insolvency, and in case of his failure to so attend and submit to an examination the burden of proving his solvency shall rest upon him."

By the first sub-division marked (*a*) of this section, acts of Bankruptcy are made to consist of certain acts of the debtor,

listed under five heads. Unless some one of these has been committed, the debtor cannot be adjudicated a bankrupt, however insolvent he may be. By the second sub-division marked (*b*), the right is given to creditors to file a petition in involuntary bankruptcy against their debtor, "who is insolvent and has committed an act of bankruptcy." This clearly requires the existence of both facts to justify the adjudication of a debtor as an involuntary bankrupt. By the third sub-division marked (*c*), the right is given to the debtor to defend the petition of his creditors, by pleading and proving that, at the date of the filing of said petition, he "was not insolvent, as defined by this act," and if he proves his plea, the petition shall be dismissed. Substitute for "insolvent" in these sub-divisions its definition as fixed by the act, and our position is made clear.

The distinction between insolvency and acts of bankruptcy, is made clear, and their concurrence made necessary, also, in Chapter V of the Act of Congress, which provides, Section 18 (*d*): "If the bankrupt, or any of his creditors, shall appear, within the time limited, and controvert the facts alleged in the petition, the judge shall determine, as soon as may be, the issues presented by the pleadings, without the intervention of a jury, except in cases where a jury trial is given by this act, and make the adjudication or dismiss the petition."

"Sec. 19. *Jury Trials*, a. A person against whom an involuntary petition has been filed, shall be entitled to have a trial by jury in respect to the question of his insolvency, except as herein otherwise provided, and any act of bankruptcy alleged in such petition to have been committed, upon filing a written application therefor at or before the time within which an answer may be filed. If such application is not filed within such time, a trial by jury shall be deemed to have been waived."

By Sec. 30. This court is directed to prescribe the necessary rules, forms and orders as to procedure, and for carrying the act into force and effect. This has been done, and "Gen-

eral orders and forms in bankruptcy," so prescribed, are printed as Appendix to Volume 172, U. S. R.

In the form of petition by creditors (pp. 681–2) they are required to state "that said (their debtor) is insolvent, and that within four months next preceding the date of this petition, the said (their debtor) committed an act of bankruptcy, in that he did," &c. In the form for pleading by the debtor (p. 684) he denies, that "he has committed the act of bankruptcy set forth in said petition, or that he is insolvent," &c. These forms are a judicial construction by this court of the provisions of the act recited, for to frame the said forms of procedure in pleading the court of necessity must have construed the provisions of the act as to pleading.

That under the act now in force two things must concur to adjudicate an involuntary bankrupt, to wit: insolvency and committal of an act of bankruptcy, seems clear by the language of the act, and by the construction put upon it by this court in the forms of pleading prescribed by it. This being so, to answer the question presented to this court in the negative, and to hold that a debtor who has made a general assignment for the benefit of his creditors, is thereby denied the right to plead and prove his solvency, the court must find some provision of the act making such an assignment an exception to the requirement of Sec. 111, sub-division *b*, above recited, and dispensing with the element of insolvency required by that sub-division, or that such a deed necessarily implies insolvency, within the meaning of the act. There is no provision of the act making such an exception, and such a deed does not necessarily imply insolvency as defined by the act. We have seen that a person is only insolvent, as the word is used and defined by the act, when his property shall not, at a fair valuation, be sufficient in amount to pay his debts, exclusive of the property, if any, involved in an attempt to defraud creditors. No such attempt is alleged here. A debtor may become involved so as to make it best for himself and his creditors, that he should avoid litigation, and forced sales under threatened judgments,

and priorities, by making a general assignment for the benefit of all creditors, and yet have property more than sufficient to pay his creditors at a fair valuation.

Such cases, though rare, are in the experience doubtless of the court, and the possibility of solvency is provided for in the deed in question, by the provision, that after the payment of creditors and expenses out of assets, "the balance, if any, to be paid to the party of the first part (the grantor) or its assigns."

It will be seen, also, that to hold that the making of a general assignment for the benefit of all creditors, is conclusive evidence of insolvency, within the meaning of that word as used in the act, is to amend and enlarge the definition of the word as fixed by the act.

The act limits the meaning of the word to the condition of a debtor whose property is insufficient, at a fair valuation, to pay his debts. The contention of the appellees would require the addition of the words, "or the making of a general assignment for the benefit of creditors."

Let us examine now the grounds taken by the appellees.

In order to sustain their position the learned counsel for the appellees limit the right to plead insolvency to subdivisions *b* and *c*., chap. 111, and construe these subdivisions to refer merely to the first three acts of bankruptcy, designated in subdivision (*a*), under the numerals (1), (2) and (3), and exclude the right of defense, on the ground of solvency, from the acts designated under the numerals (4) and (5). In order to reach this conclusion they make the word "subdivision," refer to the parts of the section indicated by numerals, and not to those indicated by letters. This, we contend, is plainly error. The sections are divisions of the chapters of the Act, and the several paragraphs into which the sections are divided are subdivisions of those sections. That such was the meaning of the act is seen by comparing the different parts of this section. If the numerals were referred to as marking the subdivisions of the section, they would be numbered continuously through the section, and yet we find these numerals reaching (5) in

subdivision (*a*), and commencing again with (1) in subdivision (*b*). The same arrangement of the numerals appear in subdivisions of other sections; for example, in sec. 39, where (*a*) has 9 numerals, and (*b*) has from (1) to (3). Again, the words of subdivision (*b*) apply to all acts of bankruptcy, and require insolvency to concur with any and every one of them. "A petition may be filed against a person who is insolvent and who has committed an act of bankruptcy." No distinction is made in the acts of bankruptcy.

That the letters by which the section is subdivided are to be taken as representing the numbers of the subdivisions is plain from the language of subdivision (*c*). "It shall be a complete defense to any proceedings in bankruptcy instituted under the first subdivision of this section," &c. When we look to the subdivision indicated by (*a*), which is the first, we find that the acts of bankruptcy indicated, and divided by the numerals, stand in different relations to insolvency as an essential to the mere act of bankruptcy. (1) makes an attempt to defraud creditors an act of bankruptcy, without insolvency, and so does (4) regarding the general assignment for the benefit of creditors. The preference given, or allowed to be gotten, in favor of some of his creditors, recited in (2) and (3), is not an act of bankruptcy, unless the debtor was at the time insolvent. As against all of these, we contend, the act allows a defense of solvency. As to (5), that makes a case of confessed insolvency and a waiver of defense, or a case of mistake of the debtor as to his condition when he made confession. Why should Congress allow this privilege of pleading solvency to the debtor who has defrauded his creditors, and deny it to the honest debtor, who gave a preference, believing himself solvent? This would be offering a premium for actual fraud, which is plainly distinguished from technical fraud by the act. That this is error in the construction is made plainer by sub-division (*d*), which provides for the production of the debtor's books, papers and accounts, on the trial of his plea of solvency; "whenever a person against whom a petition has been filed, as hereinbefore provided under the

second and third subdivisions of this section, takes issue with and denies the allegation of his insolvency." The second subdivision, marked (*b*), alone gives the right to file the petition treated of, and the third subdivision, marked (*c*), gives the right to plead solvency to said petition. Subdivision (*a*) gives no right to file a petition or to plead; it is plain, therefore, that no part of (*a*) is alluded to. It is also plain that the debtor should be liable to examination upon his books, &c., on every plea of solvency, and no reason can be conceived why any distinction should be made as to this between the cases in which he so pleads. Yet the learned counsel, by their construction, make the act require the production of books and papers, when the debtor has given, or allowed, a preference, but does not require such production when he plays the rascal, and attempts to defraud his creditors. Such could not be the meaning of the act. To construe the subdivisions of section 3 as indicated by letters, commencing with (*a*), and afterwards referred to as first, second and third subdivisions, makes the section intelligible and harmonious in its parts, and with the sections in chapter IV quoted, regulating pleadings generally.

Justice Brown, *in re Gutwillig*, 475 Fed. Rep., January, 1899, takes this view of the enumeration of the subdivisions of the chapters by letters, making (*a*) as (1)st, (*b*) as (2)nd, and so forth.

The learned counsel for the appellees have argued in the lower courts, that this treatment of the subdivisions of Chapter III in their enumeration would produce inconsistency, in that by the acts of bankruptcy numbered (2) and (3), section 3, the insolvency required must be cotemporaneous with the preference given or allowed by the debtor, while by subdivision (*c*) of section 3, the plea is solvency at the time of filing the petition against him. But these are not irreconcilable. A debtor may have been insolvent when he gave or allowed a preference, and have become solvent when the petition is filed; for the filing is allowed within four months after the recording or registering of the instrument by which the preference is given,

or allowed, and such record or registering may be delayed for an indefinite time.

It seems, therefore, that it is the intention of the act to provide by subdivisions (*c*) and (*d*) of Chapter III, special defenses and procedures for solvent debtors, but not to conflict with the general provisions for defenses contained in Chapter IV. The court will always construe an act so as to make it harmonious, if possible, and will not take away the privileges of debtors, under Chapter IV, unless in direct conflict with some other provision of the act.

In the case of *in re Gutwillig* (*supra*) the plea of solvency was not interposed, and the question here was not, therefore, involved.

Justice Brown held *in re Gutwillig* (*supra*), that a trustee appointed for a debtor declared a bankrupt, under the present act, had a right to have annulled a general assignment made by the bankrupt within four months before the filing of the petition of creditors; on the ground that the administration of the assets under such assignment, interfered materially with the administration intended by Congress in the act. And for that reason the assignment must be considered a fraud upon the act. But his decision was based altogether upon the rights of the trustee after the adjudication in bankruptcy, and in no way relates to the right of the debtor to defend the petition.

Respectfully submitted,

W. W. HENRY,

Counsel for Geo. M. West Co.